

Congress of the United States
House of Representatives
Washington, DC 20515

March 30, 2023

The Honorable Gary Gensler
Chairman
U.S. Securities and Exchange Commission
100 F Street NE
Washington, D.C. 20549

Dear Chairman Gensler,

I write today to express concern regarding the Securities and Exchange Commission's (SEC) Staff Accounting Bulletin No. 121 (SAB 121). SAB 121 represents a significant departure from existing accounting treatment of assets held under custody and could preclude banks from custodying digital assets.

SAB 121 indicates an institution acting as a custodian of digital assets should "present a liability on its balance sheet to reflect its obligation to safeguard the crypto-asset" and "to recognize an asset at the same time".¹ SAB 121's treatment of digital assets differs from the existing accounting treatment of other assets held in custody, which are an off-balance sheet responsibility, and insured depository institutions already have a robust regulatory framework for the custody of assets. SAB 121 deviates from those norms and creates needless regulatory ambiguity for banks interested in providing custodial services for their customers.

I am concerned that SAB 121 goes beyond the scope of a staff accounting bulletin and establishes new obligations for public companies. The Bulletin includes a disclaimer that the statements within the SAB are "not rules or interpretations of the Commission, nor are they published as bearing the Commission's official approval".² However, SAB 121's interpretation of custody requirements for public companies differs greatly from common practice. Additionally, the Bulletin indicates there is an expectation to apply the guidance in connection with a company's financial statements no later than those "covering the first interim or annual period ending after June 15, 2022".³ Such a statement implies the SEC plans to enforce the accounting requirements set forth in SAB 121 as if they were the result of a full notice-and-comment rulemaking process. Most concerning, it is clear the SEC staff did not engage in discussions with other stakeholders including the prudential regulators. This action by the SEC is inappropriate as the SEC is not a prudential regulator and should not act as one.

¹ Securities and Exchange Commission "Staff Accounting Bulletin No. 121," April 11, 2022.

² Ibid

³ Ibid

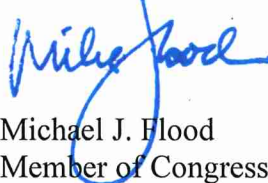
Moreover, the Office of the Comptroller of the Currency (OCC) has its own guidance regarding the custody of digital assets. Specifically, the OCC indicated that—similar to the duties involved in the safekeeping of physical assets which are done off-balance sheet—national banks are permitted to custody the keys for a customer’s digital assets.⁴ The SEC’s requirement to hold such assets on-balance sheet flies in the face of bank custody practices. As Chairman Powell said during a hearing with the Senate Banking Committee, “custody assets are off-balance sheet, always have been”.⁵ Consulting with the prudential regulators before issuing SAB 121 would have helped avoid what has become a point of regulatory ambiguity for banks.

Traditionally, assets held in custody do not directly factor into risk-based capital, leverage capital or quantitative liquidity requirements. They are neither liabilities nor assets of the custodian and do not result in additional assets or liabilities being recorded on the custodian’s balance sheet. If Question 1 of SAB 121 were to be applied to banking organizations, it could give rise to prudential requirements that would render tokenized asset and digital asset activities economically unviable for banking organizations because many regulations are triggered by, or increase in stringency based on, asset size and composition. I fear SAB 121’s requirement to put custodied assets on-balance sheet and the related knock-on effects are so burdensome that banking organizations would effectively be precluded from serving as digital asset custodians.

Excluding banks—which are already well-regulated and have decades of experience in safeguarding customer assets—from acting as custodians would not serve retail investors well. In previous speeches, you have indicated that the SEC’s objective in digital asset custody is to ensure investors’ assets are fully protected by their custodian.⁶ SAB 121 would work against this goal if it leads banks to decline to offer custodial services for their customers.

It is my belief that SAB 121 creates greater regulatory ambiguity, runs counter to longstanding practice regarding the custody of assets and goes beyond the appropriate scope of a staff accounting bulletin. I request that SAB 121 be withdrawn as written. Should the SEC choose to engage further, I request that the Commission coordinate with prudential regulators and provide for a full notice-and-comment rulemaking process.

Yours very truly,

A handwritten signature in blue ink, appearing to read "Mike Flood", is written over the printed name and title.

Michael J. Flood
Member of Congress

⁴ Office of the Comptroller of the Currency, “Interpretive Letter #1170,” July 2020.

⁵ Statements before the United States Senate Committee on Banking, Housing, and Urban Affairs 117th Congress hearing on The Semiannual Monetary Policy Report to Congress (June 22, 2022) (Jerome Powell, Chairman of the Board of Governors of the Federal Reserve System)

⁶ Chair Gary Gensler, “Prepared Remarks of Gary Gensler on Crypto Markets Penn Law Capital Markets Association Annual Conference,” April 4, 2022.